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Message Text

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ACTION EA-10

INFO OCT-01 ISO-00 SP-02 AID-05 EB-07 NSC-05 CIEP-01

TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00 COME-00

FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 LAB-04 SIL-01

AGR-05 DODE-00 PA-01 USIA-06 PRS-01 L-02 H-02 /089 W
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R 250929Z APR 75
FM AMEMBASSY SEOUL
TO SECSTATE WASHDC 9705
AMCONSUL HONG KONG

C O N F I D E N T I A L SEOUL 2930

E.O. 11652: GDS
TAGS: EFIN KS
SUBJECT: NEW FISCAL AND PRICE MEASURES

REF: SEOUL A-72

HONG KONG FOR REGFINATT

SUMMARY: ROKG HAS RAISED GOVERNMENT GRAIN AND CIGARETTE PRICES IN MOVE TO REDUCE LARGE FISCAL DEFICIT AGGRAVATED BY FURTHER INCREASE IN FERTILIZER SUBSIDY AND PROBABLE 15 PERCENT INCREASE IN DEFENSE BUDGET. PRICE CHANGES BENEFIT FARMERS AT EXPENSE URBAN WORKERS, PARTLY FOR POLITICAL REASONS, CONSUMER PRICES ARE NOW UP ABOUT 12 PERCENT BUT GOVERNMENT STILL HOPES TO HOLD TOTAL 1975 INCREASE TO 20 PERCENT. END SUMMARY

1. PRICE CHANGES: ON APRIL 15 ROKG INCREASED CONSUMER PRICES OF GOVERNMENT-HELD RICE, BARLEY AND WHEAT FLOUR BY AVERAGE OF 25 PERCENT, RAISING BOTH WHOLESALE AND CONSUMER PRICE INDEXES BY ABOUT 3.5 PERCENT. PRICES PAID TO FERTILIZER PRODUCERS RETROACTIVE TO JAN 1 ALSO INCREASED BY AVERAGE 39 PERCENT WITHOUT
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CHANGE IN PRICE TO FARMER. ON APRIL 20 PRICES ON MOST BRANDS OF CIGARETTES RAISED BY AVERAGE 47 PERCENT, WITH MAXIMUM 0.4 PERCENT EFFECT ON PRICE INDEXES. IN PRESS CONFERENCE APRIL 22 DEPUTY PRIME MINISTER

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NAM DUCK WOO SAID GRAIN INCREASES NEEDED TO REDUCE LARGE SUBSIDY DEFICIT, FERTILIZER INCREASE REQUIRED TO COVER DEVALUATION AND OTHER COST INCREASES SINCE FEB 1974, AND CIGARETTE MONOPOLY INCREASES NEEDED TO RAISE REVENUES TO HELP COVER ADDITIONAL DEFENSE COSTS AND SALARY BONUS. ALTHOUGH PRICE INDEXES NOW UP 11-12 PERCENT SINCE END OF YEAR, NAM FORECAST RELATIVE PRICE STABILITY HOLDING TOTAL 1975 INCREASE TO 20 PERCENT AND BRINGING BACK SINGLE-DIGIT INFLATION (A POST-WAR PARITY) IN 1976.

2. ALTHOUGH NOT STATED, ONE REASON FOR GRAIN PRICE INCREAS EWAS DESIRE REDUCE CONSUMPTION IN ORDER SAVE ON IMPORT BILL CURRENTLY ESTIMATED AT AROUND $500 MILLION FOR THREE GRAINS. GRAIN AND CIGARETTE INCREASE PLUS FAILURE TO RAISE FERTILIZER PRICES TO FARMERS REPRESENTS IN PART USUAL POLITICAL BIAS FAVORING RURAL OVER URBAN AREAS.

3. FISCAL DEFICITS: GOVERNMENT MOVES FORCED BY DIFFFICULT FISCAL SITUATION CAUSED PARTLY BY WORK-RELIEF EXPENDITURES BUT MAINLY BY LARGE AND GROWING GRAIN AND FERTILIZER SUBSIDY DEFICITS. TABLE BELOW (IN BILLION WON) SHOWS FIRST QUARTER DEFICITS RUNNIGN CLOSE TO BUDGER ESTIMATES FOR ALL 1975.

	BUDGET	JAN-MAR
BUDGET	- 30	- 52
GRAIN MGT. FUND	180	- 98
FERTILIZER ACCOUNT	- 90	- 85
OTHER SPECIAL FUNDS	- 30	- 20
TOTAL	-330	-255

(NOTE: FIRST QUARTER GRAIN AND FERTILIZER DEFICITS INCLUDE ABOUT 70 BILLION WON IN DEFERRED FUNDING OF CONFIDENTIAL

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1974 SUBSIDIES.)

4. FIRST QUARTER DEFICITS REQUIRED HEAVY BORROWING FROM CENTRAL BANK AND ACCOUNTED FOR 66 PERCENT OF 13.6 PERCENT INCREASE IN DOMESTIC CREDIT. GOVERNMENT REALIZES IT MUST SLOW PACE OF CREDIT INCREASE TO STAY WITHIN IMF STANDBYMID-YEAR LIMIT OF 23 PERCENT AND ENDAYEAR CEILING OF 32 PERCENT. OFFICIALS NOW TALK OF HOLDING MID-YEAR INCREASE TO 20 PERCENT TO PERMIT MORE CREDIT IN SECOND HALF WHEN EXPORTS EXPECTED TURN UP. RUNNING COUNTER TO DESIRE TO LIMIT GOVERNMENT BORROWING ARE PRESSURES FOR SUPPLEMENTAL BUDGET AND HIGHER-THAN-PLANNED

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FERTILIZER AND GRAIN DEFICITS.

5. SUPPLEMENTAL BUDGET: ROKG OFFICIALS INDICATE TENTATIVE PLAN TO SUBMIT SUPPLEMENTAL BUDGET OF 130-150 BILLION WON SOMETIME IN JULY -OCTOBER PERIOD, THIS WOULD REPRESENT 10-12 PERCENT INCREASE OVER 1975 BUDGET REPORTED REFAIR. PRINCIPAL EXPENDITURE INCREASE WOULD BE 50-55 BILLION WON OR ABOUT 15 PERCENT,ADDITIONAL FOR DEFENSE. WE HAVE NO FIRM INFO YET ON NATURE ADDITIONAL COSTS. ONLY OTHER LARGE INCREASE WOULD BE ABOUT 25 BILLION WON FOR ADDITIONAL ONE MONTH SALARY BONUS FOR CVIL SERVANTS, BRINGING TOTAL 1975 BONUS TO THREE MONTHS COMPARED ONE MONTH IN 1974. NO ADDITIONAL WORK-RELIEF EX-PENDITURES APPARENTLY BEING CONTEMPLATED AT THIS TIME. SUPPLEMENTAL REVENUES WOULD COME FROM INCREASE IN CIGARETTE MONOPOLY PROFITS (ABOUT 50 BILLION WON) AND HIGHER ESTMATES FOR TAX COLLECTIONS, WHICH ARE REPORTEDLY BEING SPEEDED UP TO REDUCE GOVERNMENT RATE OF BORROWING.

6. FERTILIZER DEFICIT: DESPITE 65 PERCENT INCREASE IN PRICE TO FARMERS LAST DECEMBER , THIS SUBSIDY WAS ESTIMATED TO REQUIRE 90 BILLION WON IN CENTRAL BANK BORROWING IN 1975, COMPARED TO 20 BILLION IN 1974. NEW INCREASE IN PRICE TO PRODUCERS WILL RAISE SUB-SIDY TO ESTIMATED 150 BILLION WON. PRICE TO FARMERS MAY BE RAISED LATE IN YEAR WHEN GRAIN PRICES PAID
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FARMERS ARE RAISED BUT PROBABLY BY LESS THAN 80 PER CENT INCREASE NOW REQUIRED TO COVER PRODUCTION COSTS.

7. GRAIN DEFICIT: THIS SUBSIDY WAS ORIGINALLY ESTIMATED AT 180 BILLION WON PLUS UP TO 20 BILLION WON IN SHORT-TERM BORROWING. CURRENT ESTIMATE IS ABOUT 240 BILLION WON BASED ON PROBABLE INCREASES OF ABOUT 20 PERCENT IN RICE AND BARLEY PRICES PAID FARMERS FOR NEW CROPS LESS ABOUT 60 BILLION WON GAINED BY APRIL 15 INCREASE IN CONSUMER PRICES. INCREASED BORROWING AUTHORITY OF AOUT 60 BILLION WON EACH FOR FERTILIZER AND GRAIN SUBSIDIES IS THUS LIKELY TO BE SOUGHT WHEN SUPPLEMENTAL BUDGET SUB-MITTED. THIS WOULD RAISE PLANNED OVERALL FISCAL DEFICIT TO RECORD 450 BILLION WON, OR TWO AND A HALF TIMES 1974 DEFICIT OF 180 BILLION WON.
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